HOUSE BUDGET COMMITTEE

Democratic Caucus

The Honorable John M. Spratt Jr. ■ Ranking Democratic Member

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June 3, 2003

Dear Democratic Colleague:

The House Budget Committee Democratic staff has just released a new report on the budget deficit. The report estimates that the total budget deficit for this year will exceed $400 billion even without the enactment of additional Republican proposals. With the added costs of the Republican "hidden agenda," total budget deficits could approach $500 billion next year, and fall only modestly before rising to near $500 billion again in 2013. Excluding the Social Security Trust Fund surplus, deficits will cumulate to $6.5 trillion over the next ten years, exceeding $800 billion by 2013 — five years after the first of the baby-boom generation begin to collect Social Security benefits. For 2002 through 2011, the budget has flipped from the Bush Administration's original projection of a $5.6 trillion surplus to a $3.6 trillion deficit — a swing of $9.2 trillion. This dramatic change in our budget prospects should be a matter of great concern to all Americans, and the Congress must weigh carefully these changed circumstances.

When President George W. Bush took office, his Office of Management and Budget, and the Congressional Budget Office, independently projected a total federal budget surplus of $5.6 trillion for 2002 through 2011. President Bush and the Republican majority in the Congress threw out the Clinton Administration's dictum to "save Social Security first," and instead proceeded immediately with a large tax cut — which they said would use only the money left over after safeguarding Social Security and Medicare, providing prescription drug coverage for the elderly, expanding the military, and paying off the national debt.

To date, the military buildup has only begun, and none of the other avowed priorities of the Republicans has even been addressed. But the 2001 tax cut has been enacted, and the projected surplus, from which the nation was to achieve those other objectives, is already more than gone.

In March of this year, the Congressional Budget Office estimated that the $5.6 trillion total federal surplus for 2002 through 2011, assuming no change in policy, has become a deficit of $377 billion. And this estimate relies upon the surplus in the Social Security Trust Fund to achieve even that worsened result. Without counting the Social Security surplus, the deficit would be $2.6 trillion. And even that dramatic erosion is not the end of the story.

The House Budget Committee Democratic staff has reassessed the state of the budget in light of the recent Treasury data on receipts and expenditures, and the state of the economy. This analysis encompasses policy proposals enacted and likely to be enacted, including the proposals in the Republican budget resolution beyond the recent tax bill, the remaining costs of the war in Iraq, the President's requests for defense and homeland security, and the repair of the ballooning individual alternative minimum tax (AMT).

The picture is very disturbing. Even with no further change in policy, the budget outlook has seriously worsened. The Treasury has reported that receipts in the crucial April tax-return filing season were far below expectations, and even worse than last year. Taking into account also the enacted tax cut and the already-passed supplemental appropriation for the Iraq war, the total budget deficit for this year will exceed $400 billion. CBO has already moved in this direction, reporting that it has increased its own forecast of the deficit from $246 billion in March to over $300 billion now.

This picture is completed with consideration of the "hidden agenda:" policies included in the President's budget that are not on the table just yet, and policies that Republicans have not yet acknowledged but are inevitable. The budget resolution did not include the President's full increase for defense, or appropriations that will realistically accommodate the likely costs of homeland security. Neither the budget resolution nor the President's budget included funding beyond fiscal year 2003 for costs of the war in Iraq (or adequate funding for Afghanistan), including reconstruction. The President has proposed, and the budget resolution included, $400 billion for a prescription drug program for the elderly. The President has proposed, and the budget resolution included, about $1 trillion of tax cuts above and beyond the enacted bill. Making the expiring provisions of the enacted bill permanent would cost $656 billion above and beyond the cost of the President's proposals. And repair of the AMT would cost at least $680 billion over the next ten years.

With all of these costs considered, the budget outlook is even more disturbing. Total budget deficits will exceed $400 billion this year, and could approach $500 billion next year. They will average almost $400 billion per year for the next ten years, and rise to $476 billion in 2013. Excluding the Social Security Trust Fund surplus, deficits will cumulate to $6.5 trillion over the next ten years, exceeding $800 billion by 2013 — five years after the first of the baby-boom generation begin to collect Social Security benefits.

For 2002 through 2011, the budget has flipped from the Bush Administration's original projection of a $5.6 trillion surplus to a $3.6 trillion deficit — a swing of $9.2 trillion. The President said that he would pay off the entire public debt by 2011; instead, the staff analysis projects publicly held debt will reach $7.0 trillion by that year. As a percentage of the GDP, the public debt will jump to 44 percent — up by one third from just two years ago, and wiping out most of the progress achieved by the Clinton Administration. By 2013, when the Republican budget resolution projects a debt subject to statutory limit of $12.0 trillion, our analysis suggests instead that the statutory debt will be $14.7 trillion — well over double the amount today, and almost triple the size that President Bush inherited two years ago.

These are not empty figures. Deficits and debt do matter. And they matter especially now, on the dawn of the era of the retirement of the baby boom, and the radical demographic change arising from the enduring phenomena of increased longevity and reduced family sizes. When the full force of the retirement of the baby boom hits both Social Security and Medicare, the federal government will have no budgetary resources to respond to any adverse developments — whether related to population aging, national security, natural disasters, or any other contingency.

Some apparently think that the best course for this nation is to cut taxes to the greatest extent that is politically possible in the heat of this moment, so that when we reach future budget contingencies there will be the greatest possible pressure to cut federal spending. But this view is irresponsible. We are all thankful that America could address the crisis of September 11 and its aftermath from a position of budgetary strength; and we should consider it our responsibility to restore that budgetary strength for the next contingency — be it national security, education, the aging of the population, or any other priority. And Members should understand that if the Congress cuts taxes but does not cut spending on widely accepted national priorities in the face of a contrived budget emergency today, then the result will be still more deficits, still more debt, reduced private-sector business investment, slower productivity growth, reduced prosperity, and a burden of debt weighing on our children's future.

Sincerely,
/s
John M. Spratt, Jr.
Ranking Democratic Member

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May 29, 2003

A Ten-year Economic Outlook

Short Summary

The budget's bottom line deteriorates to a $416 billion unified deficit in fiscal year 2003 and a $489 billion deficit in 2004. Not counting the Social Security Trust Fund surplus, deficits are $579 billion in 2003 and $662 billion in 2004.

The ten-year unified deficit, 2002 - 2011, is $3.621 trillion - a swing of more than $9 trillion from the $5.6 trillion surplus projected over the same period two years ago. The cumulative non-Social Security deficit equals $5.863 trillion.

The accumulated debt held by the public under Bush Administration policies increases from 33 percent of GDP at the end of 2001 to 34 percent in 2002, and then rises to 37 percent in 2003 and 39 percent in 2004.

Detailed Summary

The accompanying table shows how the House Budget Committee Democratic staff estimate the budget outlook for the next ten years, assuming enactment of the budget policies that Republicans have announced and begun to implement. The estimates are based on the current CBO budget baseline and economic outlook, and share CBO's assumptions that the economy will recover and grow in real terms at 3 percent per year, and that basic appropriations only keep pace with inflation. The outlook is for a budget deficit exceeding $400 billion for the current fiscal year and approaching $500 billion in fiscal 2004. The deficit improves modestly before returning to nearly $500 billion by 2013. The ratio of the debt held by the public to the GDP increases consistently through the budget window to reach 44 percent - the level when the Clinton Administration was turning the budget around in the 1990s.

The projections begin with the latest CBO baseline, issued in March of this year. From our own tracking of the budget data, we see receipts falling substantially below CBO's expected levels. We believe that by the end of the year receipts will be $67 billion below the amount

CBO anticipated. We believe that tax receipts in future years will run permanently $50 billion below CBO's March baseline, because in our judgment the transitory effect of "exuberant" financial markets on federal tax revenues has not been fully purged from the budget outlook.

The Congress has passed one supplemental appropriation to fund the Iraq war, and CBO's estimate of outlays from that supplemental is included in our projections. In addition, Congress has passed a tax cut bill, which has been signed into law by the President. Although the tax bill purports to have a revenue impact of $350 billion, revenues lost could exceed $1 trillion if the "sunset dates" in the bill are repealed, as they almost certainly will be.

Taking all of these effects into account, we estimate a new budget "baseline" with deficits of $413 billion in 2003 and $443 billion in 2004. Deficits improve thereafter because CBO assumes that the 2001 tax cuts will expire at the end of 2010 and not be renewed. Under our forecast, the budget returns to unified balance in 2011, in contrast to CBO's March baseline, which shows the budget regaining unified balance by 2008.

Thus far, the analysis includes only those policy proposals that have been enacted since March or are now under active consideration, but the Republican agenda would commit far more.

In the out years, the Bush Administration has proposed big defense spending increases and unspecified non-defense spending cuts. In our judgment, the most realistic way to represent that policy is simply to add the President's proposed defense increases to the CBO inflation-adjusted baseline. This assumes that non-defense appropriated outlays will increase only with inflation. This assumption in turn implies that all of the President's inflation-adjusted spending increases, including the international AIDS initiative and future increases for homeland security will come out of spending for other non-defense appropriations. Therefore, this estimate will probably prove to be an understatement of the Republicans' appropriations for non-defense activities.

To the assumed amount of future discretionary appropriations, we add $60 billion, divided among the next three years, for final military expenditures, economic development, and reconstruction for Afghanistan and Iraq. These costs are speculative, but there is no doubt that significant costs remain. The fiscal year 2004 budget contains only a token allowance for these costs, and the enacted supplemental was intended to cover the costs only for 2003.

To represent the full Republican tax-cut agenda, we make two adjustments. First, we add the amount needed to make permanent the "sunset" provisions of the latest tax cut bill. Second, we add the amount needed to make the 2001 tax cuts permanent. The enacted tax bill, if made permanent - in keeping with the stated objectives of the Republican leadership and the White House - would be far more expensive than its stated cost. In addition, although the tax cut bill accelerates the phase-in process for several of the provisions of the 2001 tax cut, it does not extend any of those provisions beyond their scheduled expiration (generally December 31, 2010). Also, given that both the President (in his budget) and the Congress (in the tax bill) acknowledge that the rapidly widening reach of the individual alternative minimum tax (AMT) is a serious problem, we include the cost of a moderate AMT repair. With the 2001 tax cuts made permanent, the number of households forced to pay the AMT would jump from 1.5 million in 2001 to about 39 million by 2012, according to the Administration. The remedy included in this projection is modeled on an approach developed by Leonard Burman and William Gale, under which the reach of the AMT in 2012 would extend still to about 6 million taxpayers.

Finally, our estimate includes the Administration and the Republican budget resolution's funding to provide prescription drug coverage to the elderly, $400 billion over the next ten years.

When these factors are included, the budget's bottom line deteriorates to a $416 billion unified deficit in fiscal year 2003; a $489 billion deficit in 2004; deficits no smaller than $329 billion in 2007, rising again to $476 billion in 2013. The cumulative deficit over the ten-year budget window from 2004 through 2013 is $3.959 trillion. Not counting the Social Security Trust Fund surplus, the deficits are $579 billion in 2003, $662 billion in 2004, falling only to $557 billion in 2006, and then rising again to $807 billion in 2013. The cumulative non-Social Security deficit over 2004 through 2013 is $6.527 trillion.

The 2002 through 2011 ten-year unified deficit is $3.621 trillion - a swing of more than $9 trillion from the projection of a $5.6 trillion surplus over the same period as of two years ago. The cumulative non-Social Security deficit is $5.863 trillion.

The accumulated debt held by the public under Republican policies increases from 33 percent of the GDP at the end of 2001 to 34 percent in 2002, goes to 37 percent in 2003, and 39 percent in 2004, and rises ultimately to 44 percent of GDP at the end of 2013.

The bottom-line: We are about to leave the next generation an enormous legacy of debt, stacked on top of the burden of sustaining Social Security and Medicare. And while the Bush Administration's tax cuts may stimulate the economy now, the deficits they produce will run up the cost of capital and stifle growth in the future.

BUDGET OUTLOOK WITH CONFERENCE TAX CUTS

CBO Assumptions, Fiscal Years, Billions of Dollars; Surplus Is Positive

March 2003 Baseline	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
Unified Surplus	-158	-246	-200	-123	-57	-9	27	61	96	231	405	459	891	-377
On-Budget Surplus	-317	-408	-373	-317	-269	-240	-224	-207	-190	-73	88	128	-1,678	-2,619
Off-Budget Surplus	160	163	173	195	212	231	250	268	286	304	318	331	2,568	2,241
Technical Reestimate	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
Receipts	0	-67	-59	-54	-52	-51	-51	-50	-50	-50	-50	-50	-517	-484
Legislation	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
Iraq War Supplemental	0	-38	-27	-7	-1	0	0	0	0	0	0	0	-36	-75
Conference Tax Cuts	0	-61	-149	-82	-21	-14	-17	-11	-4	4	3	2	-289	-354
Subtotal	0	-166	-234	-144	-74	-65	-67	-62	-54	-46	-47	-48	-842	-913
Debt Service on Above	0	-1	-9	-22	-31	-37	-43	-49	-55	-61	-66	-73	-445	-307
Possible August Baseline	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
Unified Surplus	-158	-413	-443	-288	-162	-111	-84	-49	-13	124	292	338	-396	-1,596
On-Budget Surplus	-317	-576	-616	-483	-374	-342	-334	-317	-300	-179	-26	6	-2,965	-3,838
Omitted Costs	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
DISCRETIONARY														
Bush Defense Increase	--	0	0	-2	-8	-13	-22	-28	-32	-34	-36	-38	-212	-139
Further Cost of War	--	0	-30	-20	-10	0	0	0	0	0	0	0	-60	-60
REVENUES														
Extend Conference Agreement	--	0	-1	-15	-78	-78	-71	-72	-82	-85	-86	-89	-656	-480
Bush Tax Cut (Over Conference)	--	-3	-10	-23	-27	-32	-37	-47	-46	-180	-283	-296	-981	-404
AMT Repair	--	0	-4	-12	-27	-41	-56	-73	-89	-107	-126	-146	-680	-408
MANDATORY														
Medicare Rx	--	0	0	0	-22	-34	-39	-44	-50	-63	-70	-78	-400	-252
Total Change	0	-3	-45	-71	-172	-197	-225	-264	-299	-468	-601	-647	-2,989	-1,744
Debt Service on Above	0	0	-1	-4	-11	-22	-34	-50	-68	-92	-126	-167	-574	-281
RESULTING DEFICIT	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
Unified Surplus	-158	-416	-489	-364	-345	-329	-343	-363	-380	-436	-435	-476	-3,959	-3,621
On-Budget Surplus	-317	-579	-662	-558	-557	-560	-594	-631	-666	-740	-753	-807	-6,527	-5,863
DEBT HELD BY THE PUBLIC	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2004-2013	2002-2011
CBO 2001 Baseline Debt	2,870	2,537	2,157	1,738	1,246	682	54	-651	-1,444	-2,314	N.A.	N.A.	N.A.	N.A.
CBO Current Baseline Debt	3,540	3,766	3,927	4,013	4,045	4,034	3,983	3,894	3,766	3,501	3,062	2,565	N.A.	N.A.
Debt With Policy	3,540	3,956	4,445	4,809	5,154	5,483	5,826	6,189	6,568	7,004	7,439	7,915	N.A.	N.A.
Difference	670	1,419	2,288	3,071	3,908	4,801	5,772	6,840	8,012	9,318	N.A.	N.A.	N.A.	N.A.
Debt With Policy, % of GDP	34%	37%	39%	40%	41%	41%	42%	42%	42%	43%	44%	44%	N.A.	N.A.

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29-May-03